John Dessauer Investments, Inc.

www.johndessauerinvestments.com

John Dessauer's market review and update as of Wednesday September 23, 2015

Last week, by a 17-13 vote, the U.S. Federal Reserve decided to leave short term interest rates near zero. Stock markets in emerging economies rose after the news. Stocks in the U.S. and other developed economies went down. Investors in emerging markets were relieved. Their fear had been that higher U.S. interest rates would result in capital outflows like 1997. Investors in developed economies sold stocks because of fear the global economy was slowing more than expected. What all investors missed was a very important statement by Federal Reserve chair Yellen. The Federal Reserve did not have to tighten monetary policy because the markets were doing that for them.

She said the global outlook has appeared to become less certain, adding that recent falls in U.S. stock prices and a rise in the value of the dollar were already tightening U.S. financial market conditions. Goldman Sachs estimates that tighter financial market conditions are equivalent to raising interest rates by 0.75% percentage points, about three times what was expected of the Federal Reserve. Goldman Sachs went on to say that tighter financial market conditions could well slow the economy down and, as a result, put even less upward pressure on inflation. In other words interest rates may stay low for a lot longer than many expect.

The good news - that investors will soon realize - is that the Federal Reserve is sensitive to stock market conditions and does not like the selloff in China, the U.S. and

other stock markets. Central bankers do not like financial market bubbles, but they know that dangerous bubbles develop when there is a surge in credit. If anything, economies in Europe and the United States are struggling because of inadequate credit formation. Businesses small and large are having a hard time getting the financing they need.

As can be seen from the vote, there is a substantial number of experts who see the U.S. economy as strong enough to need higher interest rates. Among those who agree with the decision to keep interest rates near zero, most are concerned about conditions outside the U.S. - in China, slow growing Europe and Japan. While they are not getting much attention, there are also serious lingering soft spots here at home.

After six years of recovery and media spin about job creation and falling unemployment, you might expect the U.S. poverty rate to be declining. However despite a sharp drop in the unemployment rate, the nation's poverty rate showed no improvement last year and the typical American household, once again, showed no real gain in income.

The Census Bureau's annual figures on income and poverty, released last Wednesday, came as a disappointing surprise to all who believed the media spin about a tightening labor market and improving economy. The Bureau's report said the share of Americans living in poverty was 14.8% last year, a slight increase from 14.5% in 2013 and well above the pre-recession12.3% in 2006. Last year the number of individual Americans living in poverty rose to a new record 46.7 million. The poverty line last year was $24,008 for a family of two adults and two children. In addition, American households made no headway in the long-term problem of stagnant incomes. Despite gains in the number of people holding full-time jobs, the median household income

declined last year to $53,700 from $54,462 in 2013. There are pockets of opportunity in the United States, but there are far more places where the economic recovery has been so small as to *increase* rather than decrease the number living below the poverty line. Clearly, the U.S. has a long way to go before underemployment is resolved and Americans start to see real gains in incomes. The rise in poverty here at home may not have attracted media attention, but it is a good reason to keep interest rates low.

Reuters reports that one member of the U.S. Federal Reserve at last Thursday's meeting not only did not want interest rates raised - he called for a new low or negative interest rate to insure against stalled incomes and low inflation acting as a further drag on the economy. The Bank of England's chief economist, Andy Haldane, who has been worried about the long term sustainability of the global economy, said after last Thursday's U.S. interest rate decision that central bankers need to accept that interest rates might get stuck at rock bottom. There is precedent for his warning.

Interest rates have been at zero for 20 years in Japan. Japan should be a lesson for American and European politicians who favor higher taxes and more government deficit spending. Japan has done both (Japan's government debt is 246% of GDP), but has not been able develop sustainable economic growth. After 20 years you would think Japan's economists and politicians would change course, reform taxes, reduce regulation, and make small business financing more available. The current prime minister has made efforts in that direction, but 20 year old habits have proven hard to break. Japan's economy appears to be stalling again.

A top European Central Bank Official said the ECB's bond-buying program might need to be rethought if low inflation becomes entrenched. But he added that monetary policy would not restore economic growth over the long term. Our own central bank leaders have said the same thing repeatedly since the recession of 2008 began. Former Federal Reserve chair Bernanke told members of Congress over and over again that the economy was suffering from fiscal headwinds that they needed to address. The current chair Janet Yellen has repeated Bernanke's comments during her Congressional testimony. But, we hear leading candidates from both parties talk about raising taxes, adopting protectionist policies and imposing more restrictions on Wall Street financiers. There are voices talking about helping small businesses, encouraging entrepreneurs and reforming taxes, but they are overwhelmed by media favorites. Hopefully taxes and the economy will rise to the top of popular issues by next November.

Meanwhile the U.S. and other developed world stock markets have overreacted. They have fallen as if the world were sinking into a new recession. While that is a long term risk, it is not the current reality. The U.S., British and European economies are growing. The U.S. and British are leading the pack. As our Federal Reserve proved last week, Central bankers are not going to put their stock markets at risk by raising interest rates. Stocks remain our best investment choice.

I will have the next market review and update for you one week from today on Wednesday September 30, 2015.

All the best,

John Dessauer ©September 2015